



African Forum and Network
on Debt and Development

Campaigning on Illegitimate Debts Lessons, Prospects and Proposals

By Charles Mutasa¹

1.0 Introduction and Context

Although the expression, "illegitimate debts" has gained some popularity among NGOs, it is not (yet) a term that has gained currency in official circles. However, a conference like the NGOs International Conference on Cancellation of Illegitimate Debts convened end of May, 2006 in Jakarta, Indonesia offered a chance to coin this term, to determine what, precisely, is to be understood by illegitimate debts.

In general the term "illegitimate" means "against the law, illegal or not authorized by law; improper" or "wrongly inferred" and to some extent "illogical". Defined thus illegitimate debts include odious debts, loans secured through corruption, usurious loans, and certain debts incurred under inappropriate structural adjustment conditions. Having this perception and understanding, it therefore becomes justifiable that the people of the impoverished South should not be obligated to pay debts acquired by governments where creditors knew the debts were illegitimate. Creditors who lent to the corrupt regimes of Mobutu Sese Seko of Zaire (Now Democratic Republic of the Congo), Suharto of Indonesia, Marcos of the Philippines (just to mention a few) should bear the risk attributable to their decision to finance the self-enrichment (at the expense of the country) of "their man" during the Cold War era/otherwise.

The term illegitimate debt does not exist in the legal fraternity except in the court cases given by Alexander Sacks who theorized the concept. Joseph Hanlon then referred to loans being illegitimate: "We consider loans to be illegitimate if: they are against the law or would be against national law; are unfair, improper or objectionable; or infringe upon public policy"²

Hanlon went on to develop four categories of illegitimate Debt namely: unacceptable loans; unacceptable conditions; inappropriate loans; and inappropriate conditions³. Unacceptable loans or conditions are those that are prima facie void because the original loan involved clear misconduct by the lender, violated the national law of the debtor, or was grossly unfair. This involves corruption, poor policy advice or environmentally damaging projects and capital flight. Inappropriate loans or conditions are those that the lender failed to apply prudence and due diligence and gave a loan that was inappropriate under the circumstances. This includes illegally (according to national law) lending money at excessively high interest and loans for consumption purposes.

1.1 The Doctrine of Illegitimate Debt

If a despotic power incurs a debt not for the needs or the interest of the state, but to strengthen its despotic regime, to repress the population that fights against, etc., this debt is odious for the population of all the state - Sack, Alexander Nahum, 1927, Paris.

The role and contribution of Alexander Sack, the professor of law in Paris, in his 1920s codification of the Doctrine of Illegitimate Debt has been well recognized. According to Alexander Sacks who theorized the doctrine of Illegitimate Debt; "If a despotic power incurs debts not for the needs or in the interest of the state, but to strengthen its despotic regime, to

repress the population that fights against it, or to colonize its [territories] with members of a dominant nationality, etc.... These debts are odious to the indigenous population. This debt is not an obligation for the nation, it is a regime's debt, a personal debt of the power that has incurred it." When this power falls, that debt "consequently ... falls with the fall of this power".

The Latin American Parliament developed a legal foundation characterizing four causes of illegitimate foreign debt. These include: the origin of the debt (national criminal and civil laws need to justify whether there is forgery, fraud or irregularities involved); where the creditor increases interest rates unilaterally and in unlimited fashion; the Brady Plan Agreements which forced governments of debtor countries to renegotiate debts with implicit and forced recognition of illegitimate debts, charging interest on interest; and the co-opting of government negotiators who signed agreements then resigned to assume posts in benefiting private companies from the agreements.⁵

Illegitimate debts can thus simply be classified as Debt incurred by illegitimate debtors and creditors acting illegitimately

- Odious debt or debt incurred not for the needs or interests of the state but to strengthen a despotic regime and repress the population that fights against it

- Loans which were stolen through corruption

Debts incurred for illegitimate uses:

- debts for projects which did not happen or did not benefit the people as they were intended

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² Joseph Hanlon (2002) Defining Illegitimate Debt, Understanding the Issues; Norwegian Church Aid, Norway.

³ Ibid.

⁴Quoted in Adams Patricia (1991) Odious Debts, Earthscan, London p165

⁵ Freire .P. .P. (2002) " Illegitimate Debts, Debt Relief and Citizen Audits" in CDES (2002) Upheaval in the Backyard-Illegitimate Debts and Human Rights-The Case of Ecuador-Norway, Ecuador

- debt for projects that were destructive to the community or its environment
- debt contracted for fraudulent purposes

Debts incurred through illegitimate terms:

- debt incurred with usurious interest rates
- debts that became unpayable as a result of external factors over which debtors had no control (e.g. after Northern countries unilaterally raised interest rates, or following dramatic falls in commodity prices)
- private loans converted to public debt under duress, in order to bail out lenders

Defined thus, illegitimate debt includes odious debts, loans secured through corruption, usurious loans, and certain debts incurred under inappropriate structural adjustment conditions. Picking up where Alexander Sacks left off, McGill University legal scholars relying on international custom (precedents), international conventions (such as the 1983 Vienna Convention on Succession of States in Respect of State Property), the general principles of law (such as unjust enrichment, the abuse of rights and the obligations of agents), and judicial decisions, filled in legal, financial, and political analysis to the principles of the Doctrine of Odious Debts in the 21st century. They concluded that there are three necessary conditions for a debt to be considered odious:

- 1) the debt must not have received the consent of the nation;
- 2) the funds borrowed must have been contracted and spent in a manner that is contrary to the interests of the nation, and;
- 3) the creditor must be aware of these facts.⁶

The doctrine of odious debt imposes morality on the part of international financial institutions and makes them more responsible for the purpose to which their loans might be put. Many civil society groups believe by challenging illegitimate debt they will help eliminate the moral hazard that has dominated public borrowing for the past 50 years and that has so damaged the economic, political, and social fabric of the Third World. They also believe that this will shift the balance of power in debt negotiations in favour of citizens. Lenders would take greater care to lend to governments with real authority, and not just apparent authority, and to exercise due diligence to make sure that the money is used for legitimate governmental purposes. It would go far in securing the measures required for accountable public finance that citizens throughout the South have so thoughtfully articulated. Lenders would be forced to demand evidence that the borrowing public is aware of and consents to its government borrowing before extending credit.

Briefly put, all three widely spread dictionaries subsume two kinds of debts under "illegitimate":

- a) Illegal debts, i.e. debts whose existence violates the law, basic legal principles or that are legally null and void. It would comprise debts incurred in violation of national laws, of international law, such as in breach of legal obligations or statutes of IFIs, and general universally accepted legal principles, especially debts, whose servicing violates human rights. What Jeffrey Winters (2004; see also Raffer 2004b, pp.64f) called "criminal debts" would also be illegal. These are debts from IFI disbursements to corrupt governments, such as Suharto's, knowing that large parts of these loans would be embezzled.
- b) Debts that might be legal by strictly formal standards, yet whose existence or servicing violates socially established norms.

Often, servicing them can thus not be enforced or even expected - it would be somehow "illogical" to honour them, unless the debtor is a Southern sovereign. Obviously, odious debts can be subsumed under "illegitimate", although one might discuss whether under a) or b). The evolution of the doctrine of odious debts in international law and its recent acknowledgement and corroboration in the case of Iraq would suggest subsuming it under illegal debts.

2.0. Lessons

Work that have been done on the term illegitimate debts have thus to this day brought in a number of lessons that can be used in further campaigns on the issue.

Some of the lessons are:

1. Problems with the definition, scope and contextual application of the concept.

The concept of illegitimate debt has been undisputedly put forward as having to do with authoritarian and extravagant regimes of the past rather than the present. There is no international consensus on the term "illegitimate debt" in regards to current or sitting governments of our day. It is also true that there is no reference to such a term in the international arena-at the United Nations or in the International Financial institutions. The very word "odious" does not even exist on the Paris Club homepage. It seems it remains more restricted to the world of NGOs and to few governments (mostly as a means/for the love of politicking) rather to agreed pragmatic and technical application in our global village. A case in point has been the controversial issue of Iraq debts under Saddam Hussein.

Although the odious debt doctrine has received unexpected support from the US government in the case of Iraqi debts, the concept is not clearly defined (for details cf. the locus classicus Adams 1991). What appeals most to NGOs is the rather wide interpretation in the so-called Tinoco case, which - if generally accepted - would make this concept applicable to a substantial share of sovereign debts.

Among the cases that Sacks cited in formulating his doctrine was the case of the Royal Bank of Canada, a private commercial bank, which made a loan to the outgoing dictator of Costa Rica, President Tinoco. The new Costa Rican government challenged the debt before Chief Justice Taft of the U.S. Supreme Court who was asked to sit as arbitrator. In his 1923 ruling, Chief Justice Taft noted that the transactions in question were "full of irregularities." They were also "made at a time when the popularity of the Tinoco Government had disappeared, and when the political and military movement aiming at the overthrow of that Government was gaining strength."⁷

The payments, Justice Taft discovered, were made to cover either Frederico Tinoco's expenses "in his approaching trip abroad," or his brother's salary and expenses in a diplomatic post to which Tinoco appointed him. The Royal Bank, Justice Taft ruled, cannot simply base its case for repayment on "the mere form of the transaction" but must prove its good faith in lending the money "for the real use of the Costa Rican Government under the Tinoco régime ... for its legitimate use."

According to the evidence presented, Justice Taft stated that, "The bank knew that this money was to be used by the retiring president, F. Tinoco, for his personal support after he had taken refuge in a foreign country. It could not hold his own government for the money paid to him for this purpose.

⁶ Patricia Adams (2002) *Odious Debts: The Doctrine of Odious Debts-Using the Law to Cancel Illegitimate Debt*, Germany Jubilee Network Seminar, June 2002.

⁷ Patricia Adams (1991) *The Concept of Odious debt and its relevance to Indonesia*, Probe International Press.

The position was essentially the same in respect to the payments made to Tinoco's brother." In conclusion, Justice Taft ruled, "The Royal Bank of Canada cannot be deemed to have proved that the payments were made for legitimate governmental use. Its claim must fail."

The implication of this case on debts incurred by corrupt dictators is clear. This understanding of odiousness would also comprise criminal debts.

2. The concept of odious debts also illustrates creditor domination cum arbitrariness. The only exception is in the case of Norway's acceptance and taking responsibility in its Shipping Export Credit campaign of the 1970s. The US propagated it twice: to free Cuba from Spanish colonial debts, and when Iraq was invaded.

In both cases US interest is evident. Conspicuously, this concept was neither discussed nor applied to dictators such as Somoza, Mobutu or the fascist military juntas in Chile and Argentina - all enjoying strong US support. In all these cases substantial claims of US creditors existed - unlike in colonial Cuba and Iraq.

The present discussion of odious debts and the rather thorny question of what constitutes such debts would largely have been avoided if the Rule of Law had not been waived in sovereign lending⁸.

3. It seems the world has no recent agreed precedents of illegitimate debts cancelled. The cancellation of Iraq debts by the US and the failure to extent such cancellation to other poor and needy countries has made of the concept of (illegitimate) odious debts remain contestable:

Basing a case on odiousness seems risky. Officially, Iraq's debts were not reduced because of odiousness. A CRS Report for Congress (Weiss 2005) available at an official US homepage (of the US Embassy in Italy) does not mention odiousness as the reason for US efforts to achieve debt relief for Iraq. It introduces odious debts in the following way: "Proponents of a doctrine of 'odious' debt assert that some of Iraq's debt's could potentially be classified as non-legitimate under international law since they were undertaken during the Hussein regime and that international law should be able to expunge these debts. The concept of 'odious' debt does not appear to be well established in international law." (ibid, p.6) It is conspicuous that the pertaining footnotes (omitted here) quote demands to apply "Iraqi Terms" to other debtors, e.g. S. Raghavan "African Advocates to U.S.: Reduce Our Debt Like Iraq's", in The Miami Herald of 20 February 2004. The initial opinion regarding odious debts of the US government goes completely unmentioned. What follows is thus to be expected.

"While such a commission could increase the legitimacy of a final debt restructuring plan, some believe that Iraq is not likely to seek an 'odious' debt claim. Moreover, the U.S. government has made clear its intention to restructure its Iraqi debt through the Paris Club process, and parallel negotiations with non-Paris Club countries in the Middle East and Asia, and Iraq's private creditors." (ibid.)

This source states, though: "Under traditional Paris Club guidelines, Iraq's petroleum and gas reserves would render it ineligible for debt relief." (Ibid, p.4)

⁸ Raffer Kunibert (2006) Paper presented to AFRODAD on *Implementing Fair Debt Arbitration*, Harare.

4. The "illegitimate debts" issue is well illustrated in a few specific undisputable countries and past regimes in the global South-The cases of Marcos in the Philippines, the case of DRC in Sub-Saharan Africa, the case of Argentina in Latin America are clear illegitimate cases cited.

5. The issue of illegitimacy is easily associated with:

(i) Irresponsible borrowing on the part of poor country(ies) and reckless lending on the creditor countries.

(ii) Borrowing and lending done to maintain relations between certain sitting governments and creditor governments/institutions.

(iii) Bad policy advised by the creditor institutions or countries leading to disastrous effect on the recipient country. Many severely indebted poor countries' debts, mostly owed to official sources, are largely creditor-determined, the result of creditors' decisions and monitoring. The going practice of forcing debtor countries to pay for all their creditors' failures is particularly unjustified in these cases

(iv) The stolen wealth (of Nigeria) cases which involve corrupt leaders convening with Western financial institutions to embezzle state coffers for personal gain seems also to fit into this category.

6. The absence of credible debt management units/ offices has made it a bit complicated to trace figures and trends in the affected poor countries. In many debtor countries debt records and statistics have not been properly kept to the extent that some do not know exactly how they owe. Creditors are the ones that normally tell some governments their amounts of debt and not the reverse. In such situations distinguish illegitimate and legitimate debts cannot be easy.

7. Many governments in developing countries have not added their voice to the campaign just as they have not spoken openly about bad governance of their predecessors or colleagues. Even, the Republic of South Africa (RSA) (with evidence that came from the Truth and Reconciliation Commission) had not been willing/keen to use the term "illegitimate or odious debts" or even reparations to claim compensation after apartheid. This could be an indicator that it might be very difficult for the RSA government to build a case on this concept. This does not mean, however, that campaigners should stop pointing out debts that can be defined as odious.

8. The concept seems to be more evident and easily applied when talking in historical terms rather in contemporary and future terms.

3.0 Prospects

1. There is support and conviction for the campaign as recently demonstrated by the Norwegian government deliberations. (Among creditor governments support for fair legal processes is unfortunately still extremely limited). The Kruger Sovereign Debt Restructuring Mechanism proposal within the IMF was a clear and indeed remains a clear indication that there is recognition that there are some illegitimate debt issues to be handled out there. Other sources of encouragement include the resolution of Nigeria's House of Representatives calling on the President to repudiate her debt - which in the end resulted in an unprecedented Paris Club agreement - or Argentina's unilateral cancellation of a substantial part of some debts show that debtor states, too have meanwhile gained some manoeuvring space. NGOs need to team up with as well as put pressure on their governments to repudiate illegitimate debts.

2. The Helsinki process has an opportunity of bringing up this matter as a way of promoting/introducing the rule of law into North-South relations. The question of sovereign debts and chapter 9 on a fair and transparent arbitration process has been discussed at the Helsinki Process on Globalization and Democracy that touches a lot of global governance issues.

3. Parliamentarians Support: Parliamentarians in Latin America, Italy, Germany have not only supported the need to deal with illegitimate debt but also debt arbitration and similar initiatives to address the debt question especially issues associated with bankruptcy/insolvency of the debtor countries.

The Italian Parliament (2000) passed a law on debt relief in the summer of 2000, Art. 7 under the title International Regulations on Foreign Debt that requested the setting up of consistent procedures from the International court of justice that will help in governing developing countries' foreign debt and the general framework of legal principles and human and people's rights.

During a Conference in Uruguay's Parliament the Montevideo Declaration calling for a mechanism to deal with Third Debt was formulated, and signed by Latin American Parliamentarians (available at <http://www.erlassjahr.de/content/montevideo/submit.php>). The 2000 ACP-EU Joint Parliamentary Assembly demanded "that consideration should be given to the creation of an International Debt Arbitration Panel to restructure or cancel (illegitimate) debts where debt service has reached such a level as to prevent the country providing necessary basic social services." NGOs elsewhere especially in Africa and Asia can work towards ensuring that the Montevideo Declaration is signed by their members of parliament or serve as a blueprint for a declaration taking Africa's situation more specifically into account.

4. The solidarity support of intergovernmental fora can be tapped:

The commonwealth has already upon request set up the HIPC Ministerial Forum- a platform where the IMF, the World Bank, the Paris Club and the United Nations have an opportunity to meet HIPC ministers of Finance and NGOs to discuss ways of relieving HIPCs of their debt burden. Such an opportunity and others of similar magnitude can be seized to address the illegitimate debts question.

As many African, Asian and Latin American countries are members of the Commonwealth, this is a potential platform to discuss illegitimate debts. The Commonwealth Secretariat could be approached to further the discussion on this issue. The question could also be brought up in the Commonwealth by a debtor government.

5. The UN Millennium Development Goal (MDGs) Campaign: Over decades the UN has advocated reforms of traditional debt management- if the MDGs campaign on goal 8 is centered on finding a lasting solution to the developing countries debt burden it should then be used as a starting point to demand cancellation of illegitimate debts. The UN Secretary General provided valuable inputs to the discussion, by his proposal to redefine sustainability as the level of debts allowing debtor countries to achieve the MDGs and reach 2015 without increases in their debt ratios, which he made in his Report In Larger Freedom.

6. The Financing for Development Process and the Multi-Stakeholder Meetings have moved discussion forward. At the concluding session in Geneva. The proposal to create a multi-stakeholder working group to explore additional mechanisms to improve debt workouts was widely supported and discussed at length.

Participants agreed with the proposal that the working group examine such issues as a code of conduct for sovereign debtors and their creditors, operationalization of the doctrine of 'illegitimate'/ 'odious debt,' and provision of arbitration or mediation services to facilitate dispute settlement." (UN, FfD 2005, p.9). In this regard, an opportunity exists for the 2007 Review of the Financing for Development process to put the illegitimate debts issue on the international agenda through the UN.

7. The Multilateral Debt Relief Initiative (MDRI): Initiatives such as the MDRI may facilitate the campaign for the cancellation of illegitimate debts. CSOs may simply need to put more pressure on the G8 countries to go yet another set and simply cancel debts that are illegitimate and odious though not within the HIPC framework.

4.0 Proposals

1. A coalition across the North-South divide must be built between governments in North and South willing to change the present discrimination of Southern debtors and their peoples, international organizations, parliamentarians, public servants, NGOs and the public at large, as well as private creditors interested in re-establishing the economic viability of debt distressed Southern debtors or concerned about the present plight of so many people.

2. There is need to encourage debtor governments to demand cancellation of illegitimate debts (that is rightly theirs) as they are in a very difficult position they need support and making sure that debtors who demand such are not immediately subjected to repressive reactions by official creditors. For understandable reasons the dependence of debtor governments on the goodwill (or arbitrariness) of their creditors may hinder many of them to speak up as loudly as they might wish to, and actually should. Not being debtors themselves, Organizations such as the African Union can be pressurized to take up the issue with both the United Nations and the G8 leaders.

3. Documentation and campaign: NGOs must take a lead in defining what constitutes an "illegitimate debt" as well as produce research evidence of such cases in the past and in the present. At the African Union's Experts' Preparatory Meeting in Dakar 2005, the President of the Republic of Senegal, Mr. Wade argued that any lasting solution to Africa's debt crisis must first and foremost be based on an audit - a "radioscopy" - to "make known the amount to be repaid" (AU May 2005, p.4), recognizing the principle that debt should be repaid. This is a clear call to tackle the problem of illegitimate debts and debts that would not exist in the case of debtors in the North where basic legal principles of debtor-creditor relations are respected. As the new Norwegian government declared that they would support arbitration on illegitimate debts, they might be approached whether they would be prepared to help by funding the modest costs of the documentation.

4. Establishment of a mechanism/agency to determine "illegitimate debt". The new Norwegian government proposal that:

"The Government will support the work to set up an international debt settlement court that will hear matters concerning illegitimate debt". The UN must be pressurized to establish criteria for what can be characterized as illegitimate debt, and such debt must be cancelled",

must be fully supported by the establishment of a mechanism/agency to determine this could be established within the UN in form a arbitration tribunal/court comprising elected eminent representatives of debtors and creditors on both sides and served by the UN secretariat.

This and the clear demand for canceling illegitimate debts make the Norwegian government's intentions absolutely clear. Norway's commendable readiness to introduce the Rule of Law into North-South relations is not the first case of a creditor government speaking in favour of debt arbitration or even FTAP in handling illegitimate debts. Switzerland in the 1990s tried discreetly to discuss this proposal internationally, but finally stopped these attempts as no other creditor government signalled any interest.

5.0 Conclusion

Currently the call and campaign for the cancellation of illegitimate debts may not make sense, but that's the way it should be! Campaigns by civil society have an impressive record of improving the way things are handled.

Things once declared impossible and foolish, such as the abolition of slave trade campaign and the human rights movement call against discrimination of blacks in the US in the 20th century, to cite a few cases- have become reality.

When Jubilee 2000 UK started its campaign, many doubted whether as complex an issue as international debts could be communicated to a public not really concerned about this issue. It was proved that people in creditor countries, once the sheer injustice of present structures is explained, object to present practices much more than their governments⁹. It is therefore justified, logical and human to conclude that NGOs have the right and power to make sense out of what appears to be insensible to the our governments today. It can only be public lobbying and pressure that can bring about a fair, humane and proper solution of sovereign debts. NGOs are not alone. There are parliamentarians, politicians, academics, and private creditors ready to support such demands.

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⁹Raffer Kunibert (2006) Paper presented to AFRODAD on *Implementing Fair Debt Arbitration*, Harare

About AFRODAD

AFRODAD Vision

AFRODAD aspires for an equitable and sustainable development process leading to a prosperous Africa.

AFRODAD Mission

To secure policies that will redress the African debt crisis based on a human rights value system.

AFRODAD Objectives include the following:

- 1 To enhance efficient and effective management and use of resources by African governments;
- 2 To secure a paradigm shift in the international socio-economic and political world order to a development process that addresses the needs and aspirations of the majority of the people in the world.
- 3 To facilitate dialogue between civil society and governments on issues related to Debt and development in Africa and elsewhere.

From the vision and the mission statements and from our objectives, it is clear that the Debt crisis, apart from being a political, economic and structural issue, has an intrinsic link to human rights. This forms the guiding philosophy for our work on Debt and the need to have African external debts cancelled for poverty eradication and attainment of social and economic justice. Furthermore, the principle of equity must of necessity apply and in this regard, responsibility of creditors and debtors in the debt crisis should be acknowledged and assumed by the parties. When this is not done, it is a reflection of failure of governance mechanisms at the global level that protect the interests of the weaker nations. The Transparent Arbitration mechanism proposed by AFRODAD as one way of dealing with the debt crisis finds a fundamental basis in this respect.

AFRODAD aspires for an African and global society that is just (equal access to and fair distribution of resources), respects human rights and promotes popular participation as a fundamental right of citizens (Arusha Declaration of 1980). In this light, African society should have the space in the global development arena to generate its own solutions, uphold good values that ensure that its development process is owned and driven by its people and not dominated by markets/profits and international financial institutions.

AFRODAD is governed by a Board of seven people from the five regions of Africa, namely East, Central, West, Southern and the North. The Board meets twice a year. The Secretariat, based in Harare, Zimbabwe, has a staff compliment of Seven programme and five support staff.

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